

Auditing Procedures Report

Issued under P.A. 2 of 1968, as amended and P.A. 71 of 1919, as amended.

Local Unit of Government Type <input type="checkbox"/> County <input type="checkbox"/> City <input type="checkbox"/> Twp <input type="checkbox"/> Village <input checked="" type="checkbox"/> Other		Local Unit Name Local Development Finance Authority	County HOUGHTON
Fiscal Year End JUNE 30, 2006	Opinion Date AUGUST 14, 2006	Date Audit Report Submitted to State OCTOBER 9, 2006	

We affirm that:

We are certified public accountants licensed to practice in Michigan.

We further affirm the following material, "no" responses have been disclosed in the financial statements, including the notes, or in the Management Letter (report of comments and recommendations).

YES ☒ NO ☐

Check each applicable box below. (See instructions for further detail.)

1. ☒ ☐ All required component units/funds/agencies of the local unit are included in the financial statements and/or disclosed in the reporting entity notes to the financial statements as necessary.
2. ☒ ☐ There are no accumulated deficits in one or more of this unit's unreserved fund balances/unrestricted net assets (P.A. 275 of 1980) or the local unit has not exceeded its budget for expenditures.
3. ☒ ☐ The local unit is in compliance with the Uniform Chart of Accounts issued by the Department of Treasury.
4. ☐ ☒ The local unit has adopted a budget for all required funds.
5. ☐ ☒ A public hearing on the budget was held in accordance with State statute.
6. ☒ ☐ The local unit has not violated the Municipal Finance Act, an order issued under the Emergency Municipal Loan Act, or other guidance as issued by the Local Audit and Finance Division.
7. ☒ ☐ The local unit has not been delinquent in distributing tax revenues that were collected for another taxing unit.
8. ☒ ☐ The local unit only holds deposits/investments that comply with statutory requirements.
9. ☒ ☐ The local unit has no illegal or unauthorized expenditures that came to our attention as defined in the *Bulletin for Audits of Local Units of Government in Michigan*, as revised (see Appendix H of Bulletin).
10. ☒ ☐ There are no indications of defalcation, fraud or embezzlement, which came to our attention during the course of our audit that have not been previously communicated to the Local Audit and Finance Division (LAFD). If there is such activity that has not been communicated, please submit a separate report under separate cover.
11. ☐ ☒ The local unit is free of repeated comments from previous years.
12. ☐ ☒ The audit opinion is UNQUALIFIED.
13. ☐ ☒ The local unit has complied with GASB 34 or GASB 34 as modified by MCGAA Statement #7 and other generally accepted accounting principles (GAAP).
14. ☒ ☐ The board or council approves all invoices prior to payment as required by charter or statute.
15. ☒ ☐ To our knowledge, bank reconciliations that were reviewed were performed timely.

If a local unit of government (authorities and commissions included) is operating within the boundaries of the audited entity and is not included in this or any other audit report, nor do they obtain a stand-alone audit, please enclose the name(s), address(es), and a description(s) of the authority and/or commission.

I, the undersigned, certify that this statement is complete and accurate in all respects.

We have enclosed the following:	Enclosed	Not Required (enter a brief justification)		
Financial Statements	<input checked="" type="checkbox"/>			
The letter of Comments and Recommendations	<input checked="" type="checkbox"/>			
Other (Describe)	<input type="checkbox"/>			
Certified Public Accountant (Firm Name) BRUCE A. RUKKILA, CPA, PC		Telephone Number 906-482-6601		
Street Address 310 SHELDEN AVENUE		City HOUGHTON	State MI	Zip 49931
Authorizing CPA Signature <i>Bruce A. Rukkila</i>		Printed Name BRUCE A. RUKKILA		License Number 263812

LOCAL DEVELOPMENT FINANCE AUTHORITY
HOUGHTON, MICHIGAN
HOUGHTON COUNTY, MICHIGAN
AUDITED FINANCIAL STATEMENTS

June 30, 2006

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Local Development Finance Authority
Houghton, Michigan

We have audited the accompanying financial statements of the Local Development Finance Authority as of and for the year ended June 30, 2006. These financial statements are the responsibility of Local Development Finance Authority's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

The Local Development Finance Authority has not adopted the reporting format of Government Accounting Standards Board Statement No. 34.

In our opinion, except for the effects on the financial statements for the omission described in the preceding paragraph, the dollar amount of which we have not determined, the financial statements referred to above present fairly, in all material respects, the financial position of the Local Development Finance Authority as of June 30, 2006, and the results of its operations for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated August 14, 2006, on our consideration of Local Development Finance Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

August 14, 2006

Bruce A. Rukkila, CPA, PC
Certified Public Accountants



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**REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL
REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

Board of Directors
Local Development Finance Authority
Houghton, Michigan

We have audited the financial statements of Local Development Finance Authority as of and for the year ended June 30, 2006, and have issued our report thereon dated August 14, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether Local Development Finance Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Local Development Finance Authority's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended for the information of management and federal awarding agencies and pass-through entities. However, this report is a matter of public record and its distribution is not limited.

Bruce A. Rukkila, CPA, PC

Certified Public Accountants

August 14, 2006

LOCAL DEVELOPMENT FINANCE AUTHORITY
BALANCE SHEET
June 30, 2006

	Governmental Fund Type	Account Group	TOTALS (Memorandum Only)	
	General	General Fixed Assets	2006	2005
ASSETS AND OTHER DEBITS:				
Cash	\$ 2,600	\$ 0	\$ 2,600	\$ 41,565
Accounts receivable	47,365	0	47,365	535
Prepaid expense	0	0	0	9,843
Fixed assets	0	1,673,352	1,673,352	1,577,916
TOTAL ASSETS AND OTHER ASSETS	\$ 49,965	\$ 1,673,352	\$ 1,723,317	\$ 1,629,859
LIABILITIES:				
Accounts payable	\$ 1,500	\$ 0	\$ 1,500	\$ 1,500
Payable to MTEC	0	0	0	32,712
Deferred tax revenues	33,129	0	33,129	535
TOTAL LIABILITIES	34,629	0	34,629	34,747
FUND EQUITY AND OTHER CREDITS:				
Fund balance	15,336	0	15,336	17,196
Investment in general fixed assets	0	1,673,352	1,673,352	1,577,916
TOTAL LIABILITIES, FUND EQUITY AND OTHER CREDITS	\$ 49,965	\$ 1,673,352	\$ 1,723,317	\$ 1,629,859

The accompanying notes to financial statements are an integral part of this statement.

LOCAL DEVELOPMENT FINANCE AUTHORITY
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND BALANCE
For the years ended June 30, 2006 and 2005

	<u>2006</u>	<u>2005</u>
REVENUES:		
Tax Increment Financing Revenue	\$ 193,561	\$ 138,116
Other income	6,783	0
TOTAL OPERATING INCOME	<u>200,344</u>	<u>138,116</u>
OPERATING EXPENSES		
Powerhouse Building expenses	9,928	1,500
Finlandia Portage Building acquisition expenses	85,507	72,879
Michigan Tech Enterprise Corp.- Contract Services	106,769	178,803
TOTAL EXPENDITURES	<u>202,204</u>	<u>253,182</u>
EXCESS OF REVENUE OVER EXPENDITURES	<u>(1,860)</u>	<u>(115,066)</u>
OTHER FINANCING SOURCES:		
EXCESS OF REVENUES AND OTHER		
FINANCING SOURCES OVER EXPENDITURES	(1,860)	(115,066)
FUND BALANCE, BEGINNING OF YEAR	<u>17,196</u>	<u>132,262</u>
FUND BALANCE, END OF YEAR	<u>\$ 15,336</u>	<u>\$ 17,196</u>

LOCAL DEVELOPMENT FINANCE AUTHORITY
NOTES TO FINANCIAL STATEMENTS – June 30, 2006

The Local Development Finance Authority (LDFA) of the City of Houghton and the City of Hancock was created in April, 2001 as a multi-jurisdictional LDFA. The Cities entered into this agreement governing the composition and appointment of members of the governing body of the LDFA. The area established as the LDFA District by the Cities encompasses the corporate boundaries of the cities of Houghton and Hancock.

The Authority's Board consists of seven (7) members with three appointed by the Houghton City Council, three appointed by the Hancock City Council, and one member who shall be jointly appointed by the City Council of Hancock and City of Houghton and shall be the Chair of the Board of Directors. The Authority's Board of Directors are given powers to maintain and operate the LDFA. The Authority's operations are financed substantially through a tax increment financing plan and a Michigan Economic Development Corporation grant. The Authority's purpose is to establish, implement and maintain a "SmartZoneSM" known as the Michigan Tech Enterprise Corporation- an entity for startup and nurturing of high tech commercial businesses.

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING PRINCIPLES

The following is a summary of the more significant accounting policies of the Local Development Finance Authority:

SCOPE OF REPORTING ENTITY

In accordance with the provisions of the Governmental Accounting Standards Board Statement No. 14, *The Financial Reporting Entity*, the financial statements of the Local Development Finance Authority contain all of the financial activity of the Authority's funds. The Authority is not considered a component unit of either city. Elements considered in determining that the Authority is not a component unit of the cities are as follows:

1. The Cities are not responsible for the designation of the Authority's management.
2. The Cities do not significantly influence operations.
3. The Cities each appoint three of the seven members to the Authority's Board of Directors.
4. The Cities do not have significant fiscal management responsibilities. They do not have a right to receive surplus payments made to the authority.
5. The Cities do not hold title to the physical assets of the Authority.

FUND ACCOUNTING

The accounts of the Authority are organized on the basis of funds and an account group, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues, and expenditures. The available resources are allocated to and accounted for in the individual funds based upon the purposes for which they are to be spent and the means by which spending activities are controlled. The fund utilized by the Authority is by definition a governmental fund type.

LOCAL DEVELOPMENT FINANCE AUTHORITY
NOTES TO FINANCIAL STATEMENTS – June 30, 2006

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING PRINCIPLES (Continued)

GOVERNMENTAL FUND TYPES

General Fund - The General Fund is the general operating fund and accordingly, it is used to account for all financial resources except those required to be accounted for in another fund.

BASIS OF ACCOUNTING

The basis of accounting refers to when revenues and expenditures or expenses are recognized in the accounts and reported in the financial statements. The basis of accounting relates to the timing of the measurements made, regardless of the measurement focus applied.

The governmental fund financial statements of the Authority are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenue is recognized as soon as it is both measurable and available. Revenue is considered to be available if it is collected within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Authority considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting.

Property taxes and intergovernmental grants associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenue in the current fiscal period.

All other revenue items are considered to be available only when cash is received by the government unit.

FIXED ASSETS

Fixed assets used in governmental fund type operations are accounted for in the General Fixed Assets Account Group, rather than in governmental funds. Fixed assets are valued at historical cost or estimated historical cost if actual historical cost is not available.

The General Fixed Assets Account Group is not a "fund." Its purpose is related only to the measurement of financial position and is not involved with measurement results of operations.

BUDGETS AND BUDGETARY ACCOUNTING

The Authority's annual budget is prepared in June of each year by the Board of Directors. The Authority reviews and adopts the annual budget prior to the beginning of the new fiscal year. The budget can not be finally adopted by the board of the Authority until it has the approval of both of the City Councils of Houghton and Hancock.

The Board adopts the budget on a line item basis and has the authority to amend the budget when it becomes apparent that deviations in the original budget will occur and the amount of the deviation can be determined.

The general statute governing Authority budgetary activity is the State of Michigan Uniform Budgeting and Accounting Act. The State of Michigan has enacted Public Act 621, the Uniform Budgeting and Accounting Act, to provide for a system of uniform procedures for the preparation and execution of budgets in local units of government. The main purpose of P.A. 621 is to require that all local units adopt balanced budgets, to establish

LOCAL DEVELOPMENT FINANCE AUTHORITY
NOTES TO FINANCIAL STATEMENTS – June 30, 2006

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING PRINCIPLES (Continued)

responsibilities and define the procedures for the preparation, adoption, and maintenance of the budget, and to require certain information for the budget process, including data for capital construction projects. Major provisions of P.A. 621 are as follows:

1. Local units of government must adopt a budget.
2. The budget, including accrued deficits and available unappropriated surpluses, must be balanced.
3. The budget must be amended when necessary.
4. Debt shall not be entered into unless authorized in the budget.
5. Expenditures shall not be incurred in excess of the amount appropriated.
6. Expenditures shall not be made unless authorized in the budget.
7. Violations of the act, disclosed in an audit of the financial records, in the absence of reasonable procedures, shall be filed with the State Treasurer and reported to the Attorney General.

ENCUMBRANCES

Encumbrances are defined as commitments related to unperformed contracts for goods and services. The Authority does not record encumbrances in the normal course of operating its accounting system and none are recorded in the accompanying financial statements.

TOTAL COLUMNS ON COMBINED FINANCIAL STATEMENTS

The total columns on the financial statements are captioned Memorandum Only to indicate they are presented only to facilitate financial analysis. Data in these columns do not present financial position, results of operation, or changes in financial position in conformity with generally accepted accounting principles.

NOTE B - CASH AND EQUIVALENTS

Statutory Authority

Act 217, PA 1982, authorizes the Authority to deposit and invest in:

1. Bonds and other direct obligations of the United States or its agencies.
2. Certificates of deposit, savings accounts, deposit accounts, or depository receipts of federally insured banks, insured savings and loan associations or credit unions insured by the National Credit Union administration that are eligible to be a depository of surplus money belonging to the State under Section 5 or 6 of Act 105, PA 1855, as amended.
3. Commercial paper rated at time of purchase within the three highest classifications established by not less than two standard rating services. Maturity cannot be more than 270 days after purchase and not more than 50 percent of any fund may be invested in commercial paper at any time.
4. United States government or Federal agency obligation repurchase agreements.
5. Banker's acceptance of United States banks.
6. Mutual funds composed of investments which are legal for direct investments by local units of government in Michigan.

LOCAL DEVELOPMENT FINANCE AUTHORITY
NOTES TO FINANCIAL STATEMENTS – June 30, 2006

NOTE B - CASH AND EQUIVALENTS (Continued)

Cash consists of cash on hand and the checking account.

Custodial Credit Risk - Deposits - In the case of deposits, this is the risk that in the event of a bank failure, the District's deposits may not be returned to it. As of June 30, 2006, none of the District's bank balance of \$10,680 was exposed to custodial credit risk because it was uninsured and collateralized with securities held by the pledging financial institution's trust department or agent, but not in the Authority's name.

NOTE C - GENERAL FIXED ASSETS

A summary of the changes in the general fixed assets for building acquisitions and improvements is as follows:

Building and Improvements	Balance 06/30/05	Additions	Balance 06/30/06
Powerhouse	\$ 875,103	\$ 9,929	\$ 885,032
4th floor of Portage	702,813	85,507	788,320
Total General Fixed Assets	<u>\$1,577,916</u>	<u>\$ 95,436</u>	<u>\$1,673,352</u>

NOTE D - MICHIGAN TECH ENTERPRISE SMARTZONESM AGREEMENT

A Michigan Tech Enterprise SmartZoneSM Agreement was entered into on February 7, 2002 by and among the Michigan Economic Development Corporation (MDEC), the City of Hancock, the City of Houghton, the Local Development Finance Authority and Michigan Technological University.

Michigan SmartZonesSM are collaborations between universities, industry, research organizations, government, and other community institutions intended to stimulate the growth of technology-based businesses and jobs by aiding in the creation of recognized clusters of new and emerging businesses, those primarily focused on commercializing ideas, patents, and other opportunities surrounding corporate, university, or private research institute R&D efforts.

The Cities of Houghton and Hancock, in partnership with Michigan Technological University, will support this zone, which aims to grow the high-tech job base in the Upper Peninsula. The zone will focus on nurturing biotechnology, advanced manufacturing, information technology, and earth engineering industries. It utilizes existing downtown building space in the Cities of Houghton and Hancock and the facilities on the campus of Michigan Tech, to initially create up to three incubator facilities. This agreement shall expire December 31, 2017.

NOTE E - LOCAL DEVELOPMENT FINANCE AUTHORITY AGENCY AGREEMENT

The Michigan Tech Enterprise Corporation entered into an agreement with Local Development Finance Authority (LDFA) to assume, on behalf of the LDFA, the responsibility of operating and planning the activities in connection with the terms of the Michigan Tech SmartZoneSM Agreement. The MTEC will provide administrative services, conduct integrated market studies, generate specific marketing plans, identify methods of facilitating technological commercialization, and implement an integrated marketing program. This agreement has been approved by the Michigan Economic Development Corporation.

LOCAL DEVELOPMENT FINANCE AUTHORITY
NOTES TO FINANCIAL STATEMENTS – June 30, 2006

NOTE F - TAX INCREMENT FINANCING AND DEVELOPMENT PLAN

The LDFA Board adopted a Tax Increment Financing and Development Plan on April 30, 2001. The LDFA implemented this plan under the provisions of Act 281, Public Acts of Michigan, 1986 as amended in order to develop eligible projects within the SmartZoneSM. The plan was approved by the City Councils of Houghton and Hancock. For the fiscal years ended June 30, 2006 and 2005, the SmartZoneSM captured \$226,160 and \$138,116, respectively, of tax increment revenues. The tax is levied annually with the summer school millage and will continue until the year 2017.

A summary of the TIF district data as of June 30, 2006 is as follows:

	SmartZone TIF District	
	Houghton	Hancock
Taxable base year 1999		
Real Property	63,029,631	46,361,834
Personal Property	6,221,989	3,053,010
Current year, non-homestead taxable value		
Real Property	84,226,375	59,081,799
Personal Property	6,691,485	4,361,780
Captured taxable value		
Real Property	21,196,744	12,719,965
Personal Property	469,496	1,308,770
Total captured increase of tax value	21,666,240	14,028,735
Authorized tax mills levied	11.9982	12.0000
Tax revenues levied	\$ 154,142	\$ 54,945
Less: tax revenues collected	121,543	54,945
Balance due	<u>\$ 32,599</u>	<u>\$ 0</u>

NOTE G - OPERATING RENTAL AGREEMENT

The City of Houghton Downtown Development Authority and the LDFA have an operating agreement in connection with rental income from the Powerhouse building. For any year in which there is excess rental revenues over operating and maintenance costs for the building, 12% of the excess shall be reimbursed to the DDA. If for any quarter a deficit occurs, the DDA shall reimburse to the LDFA an amount equal to the deficit. For the year ending, June 30, 2006 and 2005, a net loss of \$6,783, and a gain of \$3,850 was incurred respectively. In the prior year's report, janitorial expenses were included in the rental expenses, whereas the operating agreement states that they should not be included. In the statement below, the rental expenses from 2005 are restated to reflect the correct amounts per the agreement.

LOCAL DEVELOPMENT FINANCE AUTHORITY
NOTES TO FINANCIAL STATEMENTS – June 30, 2006

NOTE G - OPERATING RENTAL AGREEMENT (Continued)

	<u>2006</u>	<u>2005</u>
INCUBATOR REVENUES		
Powerhouse	\$ 17,352	\$ 18,505
	<u>17,352</u>	<u>18,505</u>
RENTAL EXPENSES		
Powerhouse		
Utilities	17,888	10,161
Insurance	927	907
Contract Services	2,060	0
Repair and maintenance	2,832	3,587
Small equipment and furniture	428	0
Total Powerhouse rental expenses	<u>24,135</u>	<u>14,655</u>
NET RENTAL INCOME - POWERHOUSE	<u>\$ (6,783)</u>	<u>\$ 3,850</u>

NOTE H - CONTINGENT LIABILITIES

Risk Management

The Authority is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Authority has obtained commercial insurance to handle its risk of loss.

NOTE I- RECLASSIFICATION

Certain items in the June 2005 financial statements have been reclassified to conform with the current year presentation.



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LETTER OF COMMENTS AND RECOMMENDATIONS

Board of Directors
Local Development Finance Authority
Houghton, Michigan

In planning and performing our audit of the financial statements of the Local Development Finance Authority for the year ended June 30, 2006, we considered the Authority's internal control in order to determine our auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on internal control.

However, during our audit we became aware of certain matters that are opportunities for strengthening internal controls and operating efficiency. The comments and suggestions regarding those matters follow. This letter does not affect our report dated August 14, 2006, on the financial statements of the Local Development Finance Authority.

Budget

LDFA did not comply with Public Act 621, as they did not adopt a budget for the 2005-2006 fiscal year. It is recommended that a line item budget be made for LDFA that is separate from the MTEC budget, and that the budget be presented to the City Councils of Houghton and Hancock and the Authority Board for approval.

Operating Agreement

We recommend that the operating agreement with the Cities of Houghton and Hancock be amended to increase the fiscal year reporting and determination of amounts due from our owed to the City of Houghton/DDA for annual net rental activity from 60 days to 120 days. This would allow for use of audited amounts in computing the annual net amount.

We would like to thank the staff for the excellent cooperation we received during our audit. We appreciate the opportunity to present the above suggestions.

This report is intended for the information of the Board of Directors, management, the oversight audit agency, and other federal and state audit agencies, and should not be used for any other purpose. This restriction is not intended to limit the distribution of this report, which is a matter of public record.

Bruce A. Rukkila, CPA, PC
Certified Public Accountants

August 14, 2006